No. 4254

United States

Circuit Court of Appeals

For the Ninth Circuit

In the Matter of GEORGE E. TILTON, Bankrupt.

GEORGE E. TILTON,

Appellant,

vs.

ANNA J. HELMS, ELIZABETH KEELAN, MAGDA OLSON, REBECCA S. KNIGHT, R. BLIX, FRANCES BLIX, CHRISTINA WADMAN, J. J. MIDDAL, J. STARUP, ANNA C. ADAMS, JESSIE HUMPHREY, ALICE SAXON, and RUTH SAXON,

Appellees.

Brief of Appellant

Upon Appeal from the United States District Court for the Western District of Washington, Northern Division

GEO. H. RUMMENS,
TRACY E. GRIFFIN,
Attorneys for Appellant.

612 American Bank Bldg.
Seattle, Washington.

PUGET SOUND PRINTING CO., 422 SPRING STREET

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STATEMENT OF THE CASE

This is an appeal from an order of the District Court, Neterer, Judge, denying to George E. Tilton, bankrupt, a final discharge in bankruptcy.

The record and transcript is before this court under an agreed statement by virtue of Equity Rule No. 77.

On April 26, 1921 George E. Tilton made an assignment for the benefit of creditors. At that date he delivered to the assignees property of an estimated value of approximately One Hundred Forty Thousand ($140,000) Dollars. Thereafter, on involuntary proceedings in bankruptcy, he was, on the 6th day of June, 1921, duly adjudicated bankrupt.

Claims were filed in the estate by seventy-one (71) creditors and allowed, aggregating Eighty-eight Thousand Two Hundred One ($88,201) Dollars.

On the 15th day of May, 1922 said bankrupt filed his petition for discharge. Thereupon, twenty-two (22) creditors with claims aggregating Thirty-six Thousand One Hundred Twenty-five and 65/100 ($36,125.65) Dollars, filed specifications opposing the bankrupt's discharge. Prior to the hearing Nine (9) of said creditors, with claims aggregating Twenty Thousand Eight Hundred Seventy-five

($20,875) Dollars, withdrew their objections and joined in a petition with thirty-one (31) other creditors, whose claims aggregated Thirty-one Thousand Four Hundred Fifty-nine and 19/100 ($31,459.19) Dollars, petitioning for the discharge of the bankrupt. (Trans. 4.)

The remaining eighteen (18) creditors with claims aggregating Twenty Thousand Six Hundred Sixteen and 16/100 ($20,616.16) Dollars made no objection to the discharge.

The Trustee, who was familiar with all the facts in the matter, joined in said petition for discharge. The petition was signed and supported by the three largest creditors.

At the date of hearing, the objecting creditors were Thirteen in number, with claims aggregating Fifteen Thousand Two Hundred Fifty and 65/100 ($15,250.65) Dollars.

At said hearing the objecting creditors relied upon but one specification, to-wit:

> "That said bankrupt obtained money and property on credit upon materially false statements in writing made by him to the persons (in the specifications mentioned) for the purpose of obtaining credit from such persons."

Testimony was offered and introduced relative to three series of transactions alone, involving appellees Blix, Helms, Keelan, and none other.

The Blix writing was as follows:

"23 September, 1919.

Received of R. Blix,

Seventeen Hundred par value Liberty Bonds to be returned 1 year from date, plus interest on par value at rate of 7% per annum, payable semi annually. Coupons maturing during the year to belong to undersigned. For serial number see reversed side.

(Sgd.) G. E. TILTON.

ENDORSEMENTS:

J-10295524, Victory, $100. 4 ¾% 8 coupons,
J-10295525, Victory, $100. 4 ¾% 8 coupons,
J-10295526, Victory, $100. 4 ¾% 8 coupons,
C-7309083, Victory, $100. 4 ¾% 8 coupons,
C-7309084, Victory, $100. 4 ¾% 8 coupons,
C-7309085, Victory, $100. 4 ¾% 8 coupons,
C-7309086, Victory, $100. 4 ¾% 8 coupons,
76612 2nd Issue Converted, 4¼% $500.00 2 coupons,
76613 2nd Issue Converted, 4¼% $500.00 2 coupons.

November 10, 1920, Seven One Hundred Dollar Victory Bonds returned to Mr. Blix.

G. E. TILTON." (T. 6.)

The Court held that the Blix receipt aforesaid was clearly a loan of Liberty Bonds, just the

same as a person would loan money and was not such a materially false statement in writing as would prevent a discharge.

Hence there is involved on this appeal the receipts held only by Anna J. Helms and Elizabeth Keelan.

The bankrupt obtained from Anna J. Helms in all the sum of $3300.00. The receipts, being renewal receipts, were dated October 20th, 1920, October 12th, 1920, September 20th, 1920, November 8th, 1920, November 1st, 1920, and November 11th, 1920, each in the sum of $500.00 and one September 16th, 1920, in the sum of $300.00. Each receipt, except as to date and amount above referred to, was as follows:

"20 October 1920.

Received from Anna J. Helms, Five Hundred and no/100 Dollars for loan purposes to be loaned and returned 6 months from date, plus interest at rate of 10% per annum.

$500.00.

G. E. TILTON." (T. 6.)

The bankrupt obtained from Elizabeth Keelan on October 11th, 1920, $300.00 and November 24, 1920, $200.00 upon two receipts, each identical, except as to date and amount, as follows:

"11th October 1920.

Received from Elizabeth Keelan, Three

Hundred and no/100 Dollars for loan purposes to be loaned and returned 6 months from date, plus interest at the rate of 10% per annum.

$300.00.

G. E. TILTON." (T. 6.)

The Court denied a discharge to the bankrupt because of the Helms and Keelan receipts, as above set out, and the only question upon this appeal is whether those receipts legally justified refusal of discharge under Section 14, Sub-Division "b" of the Bankruptcy Act, as amended in 1910.

The only testimony touching these receipts was that of Anna J. Helms, Elizabeth Keelan and the Bankrupt.

On direct examination Anna J. Helms testified:

"Q. Did you on March 10, 1919 loan him any money or give him any money? If so, under what circumstances?

A. Yes, I loaned him money."

She testfiied the bankrupt had been represented to her as a loan agent and he told her he loaned money and always on good security, taking only one-third the value, so she loaned him $1,000 on March 10, 1919; that she loaned in all Six Thousand and Three Hundred ($6,300) Dollars and withdrew Two Thousand ($2,000) Dollars; that originally the receipts were for six months; that the

bankrupt exchanged the One Thousand ($1,000) Dollars receipts for the Five Hundred ($500.00) Dollar receipts because he could handle them better; that he promised witness her money any time she wanted it, provided he had two weeks notice in advance; that he kept the interest payments up regularly until the bankruptcy;

That on the Three Hundred ($300.00) Dollars loan, in September, 1919, the witness examined a house boat and gave him the Three Hundred ($300.00) Dollars to loan on the house boat; that after the bankruptcy the bankrupt told the witness he had used the money personally and placed it in a general fund; that he desired to change the receipts into promissory notes and two of them had been so changed; that he paid One Hundred Ten ($110.00) Dollars upon the notes and she would not have loaned the money if she had known the bankrupt was going to put it under his own use. (T. 8.)

On cross-examination she testified that the loans were made through March to May, 1919 in One Thousand ($1,000) Dollar loans and one of Three Hundred $300.00) Dollars September 16, 1919; that the loans were placed upon a six months basis so she could draw interest for that period, although she demanded the privilege of withdrawing any part of the money she wanted on two

weeks notice; that she never examined any property on any loan except the last one of Three Hundred ($300.00) Dollars; that she never asked the bankrupt to show her any property; never satisfied a note or mortgage, nor did she make inquiry if mortgage was taken in her name;

That while she had no ill feeling toward the bankrupt, she swore to a complaint and had the bankrupt arrested on a charge of obtaining money under false pretenses, growing out of the transaction of September 16, 1919, being the Three Hundred ($300.00) loan covering the house boat; that the bankrupt was acquitted.

Elizabeth Keelan testified:

"Q. Did you during November, 1920, loan Tilton $500.00 in cash.

A. Yes, sir.

Q. Was that $500 loan made in one loan or in several loans?

A. Two."

That the bankrupt said he was a loan agent and never let out money except on good security and at one-third of the value; that shortly after the loan the bankrupt desired to change the receipts into notes; that she would not have loaned the money if she had known he was going to apply it to his own use.

On cross-examination she testified:

"Q. You said you went up and loaned him $300 and (9) then $200?

A. Yes, sir."

At the close of this testimony, the objecting creditors having rested, the bankrupt moved for a non-suit, or such other order as was proper because the objectors had failed to make out any case to resist the discharge. The motion was denied. Exception allowed. (Tr. 11.)

The bankrupt testified, on direct examination:

That he never told Mrs. Helms that he would take her money and loan it for her; that he borrowed the money from her with the understanding that he should use it in his business and that he would pay her; that he told her he was making loans and that money was coming in constantly and if she would give him reasonable time, a week or two, when she wanted money back he could always meet it. There were two or three occasions when she did come in and when he paid in advance.

Q. Did you tell her you were going to act as agent for her?

A. No. I took the money and loaned it in my name. It was loaned to me and I reloaned it."

That nothing was said about guaranteeing to her that the loan would be paid; that the money was borrowed and he agreed to pay it at the time specified.

That relative to the Lake Union houseboat, Mrs. Helms came into the office, had a headache and he told her that he was going out on a trip and suggested that she come along; that he went around to look at some pieces of property he owned and examined some property on which he had applications for loans. One was a houseboat; that he told her he had an application for the houseboat, but after examination of it he turned it down; that Mrs. Helms loaned the witness (10) $300.00 before they started on the trip and not after they came back.

That in addition to making loans, he was in the logging business and had charge of a building and loan association; that at the time these loans were made he did not then know that he was in failing circumstances; that he ascertained that fact in the latter part of January, 1921; that he had very considerable property at that time and if same had been left to him he could have paid one hundred cents on the dollar.

That originally Mrs. Helms had objected to the form of receipt and asked for notes when they first began to do business; that he agreed to notes and then she said, "Well, it doesn't make any difference. I will take this." That in January some creditors suggested the receipts might make him liable as a trust proposition and he stated he had

never understood it that way; that they had always been handled as notes and that he had handled thousands and thousands of dollars that way; that if there was any danger otherwise he wanted the legal evidence of his indebtedness put in the form which he and his creditors always understood it to be; that prior thereto other creditors had objected to the receipts and he had changed them into notes when requested. So he did go to Mrs. Helms and Miss Keelan. He stated to Mrs. Helms that as she knew, the money was loaned direct to him, and if there was any such liability as suggested, he wanted it put back on the basis of a straight loan; that never until the time of the criminal prosecution, did she claim they were anything except straight loans. (Trans. 11-13.)

On cross-examination the bankrupt testified that the money loaned by Mrs. Helms and other creditors in her position was actually used in chattel loans on personal property; that he never used any of the Helms money in his own personal business ventures; that he lost some $29,000 on chattel loans.

"Q. You considered it, in other words, a loan to you?

A. Yes.

Q. You are telling the court that those were merely loans to yourself personally?

A. That is the way we understood it at the time.

Q. Why did not you give notes then?

A. I did in many cases." (Trans. 13-14.)

That he had carried on his own business transactions in this manner for a great number of years; that he never represented he was acting as agent for other parties; that the people to whom he made loans understood that they were dealing with the bankrupt alone.

At the close of this testimony, there being no rebuttal, the bankrupt renewed the motion for discharge, which was, by the Court, denied. (Trans. 14-19.)

Thereafter, on the 8th day of May, 1924, the Court did enter a formal order denying a discharge to the bankrupt, reciting in part:

> "And the court having heard the evidence in said cause, and finding that the objections to the discharge on the part of two of said creditors only, namely Anna J. Helms and Elizabeth Keelan, were well taken, said objections were by the Court sustained. * * * *" (Trans. 20-21.)

SPECIFICATIONS OF ERROR

I.

That the Court erred in denying the bankrupt

his final discharge from any and/or all debts and claims which are made provable by said Act of Bankruptcy against his estate and which existed on the 25th day of May, 1921, on which day the petition for adjudication was filed.

II.

Because said order or decree denies to the bankrupt his discharge in bankruptcy as sought.

III.

Because said decree or order denies to the bankrupt his discharge for causes not specified in Section 14, Sub-Division "b" of the Bankruptcy Act, as amended in 1910.

IV.

Because said order or decree denies to the bankrupt his discharge based upon Section 17 of said Act.

V.

Because said order or decree denies his discharge only because of a receipt, the body of which, omitting names, dates and amounts, is as follows:

"Received from.....,
.....Dollars for loan purposes, to be loaned and returned six months from

date, plus interest at 10% per annum."

and all testimony in the case shows that said transactions were direct loans to the bankrupt and said receipt is not such character of instrument in writing as is contemplated by the Bankruptcy Act, to constitute a materially false statement in writing, and the bankrupt did not obtain money or property or credit upon any materially false statement in writing made by him to either of said objecting creditors.

VI.

Because the Court should have granted the bankrupt's motion for discharge at the close of the case of the objecting creditors, and granted bankrupt's motion for non-suit therein.

VII.

Because said order or decree denies to the bankrupt his discharge as to all debts of every nature and description made provable by said Act against his estate which existed on the 25th day of May, 1921, although the objections filed were sustained as to but two creditors only.

ARGUMENT

As stipulated in the agreed statement under Equity Rule No. 77, at page 7 of the Transcript of Record, *the only question upon this appeal is whether the Helms and Keelan receipts legally jus-*

tify refusal of discharge under Section 14 *in Sub-Division "b" of the Bankruptcy Act as amended in* 1910.

Specifications of error I to VI inclusive fall under one heading and, to facilitate the argument, will be discussed as one, insasmuch as they each deal with the refusal to discharge the bankrupt because of the receipts herein involved—that is, the objection made here is that the bankrupt obtained money or property on credit upon a materially false statement in writing made by him to either said Helms or Keelan for the purpose of obtaining credit from such person or persons.

Section 14, Sub-Division "b" of the Bankruptcy Act, as amended in 1910 (Comp. St. 9598) is as follows:

> "The judge shall hear the application for a discharge and such proofs and pleas as may be made in opposition thereto, by the trustee or other parties in interest, at such time as will give the trustee or parties in interest a reasonable opportunity to be fully heard, and investigate the merits of the application and discharge the applicant unless he has (1) committed an offense punishable by imprisonment as herein provided; or (2) with intent to conceal his financial condition, destroyed, concealed, or

failed to keep books of account or records from which such condition might be ascertained; or (3) obtained money or property on credit upon a materially false statement in writing, made by him to any person or his representative for the purpose of obtaining credit from such person; or (4) at any time subsequent to the first day of the four months immediately preceding the filing of the petition transferred, removed, destroyed, or concealed, or permitted to be removed, destroyed, or concealed, any of his property, with intent to hinder, delay, or defraud his creditors (5) in voluntary proceedings been granted a discharge in bankruptcy within six years; or (6) in the course of the proceedings in bankruptcy refused to obey any lawful order of, or to answer any material question approved by the court: Provided, That a trustee shall not interpose objections to a bankrupt's discharge until he shall be authorized so to do at a meeting of creditors called for that purpose."

Subdivision 3 of said paragraph "b" was not in the original Act, but added by the amendment of 1910, so that the only objection to discharge is that now found under sub-division 3,—that is:

"Obtained money or property on credit upon a materially false statement in writing, made by him to any person or his representative for

the purpose of obtaining credit from such person;"

The receipts upon which it is claimed credit was obtained in this case are not the statements referred to in the Act, such as to prevent a discharge. It may be true that upon the bankrupt being discharged, the debt evidenced by those receipts will not be affected by the discharge under Section 17, subdivisions 2 and/or 4.

Section 17 is as follows:

> "A discharge in bankruptcy shall release a bankrupt from all of his provable debts, except such as . . . . (2) are liabilities for obtaining property by false pretenses or false representations . . . . ; or (4) were created by his fraud, embezzlement, mis-appropriation, or defalcation while acting as an officer or in any fiduciary capacity."

Hence there must be kept in mind the distinction between Section 17 governing *debts not affected by discharge, and* Section 14-b, governing the *causes which prevent a discharge.* The fact that certain debts are not affected by a discharge, shows upon the face of the statute that the mere fact of such debts existing, does not prevent the discharge. The discharge can be denied only for those causes set forth in the statute under Section 14-b. This statute must be strictly construed in favor of

the bankrupt. Hence, the fact, if it be a fact, that the receipts in evidence here were used by the bankrupt as a false pretense and a false representation in obtaining credit, or that as agent he embezzled or misappropriated the money to his own use, would not and will not bar the discharge.

As heretofore stated, the receipts and the writing therein contained are not the "Materially false statement in writing" referred to in Section 14-b.

A FALSE STATEMENT ON WHICH A BANKRUPT OBTAINS MONEY OR PROPERTY ON CREDIT WHICH WILL BAR HIS DISCHARGE UNDER SECTION 14 B, SUBDIVISION 3 MUST BE A *"FINANCIAL STATEMENT"* AS DISTINGUISHED FROM A MERE REPRESENTATION.

In re Morgan, 267 Fed. 959;
In re Lundberg, 272 Fed. 107;
In re Robinson, 266 Fed. 970;
In re Hudson, 262 Fed. 778;
In re Rea Bros., 251 Fed. 431;
In re Tanner, 192 Fed. 572.

In the *Morgan* case, *supra,* stock was sold upon a prospectus which was false, and the following receipt given:

"No. 17 Subscription Receipt 30 Shares
"Iowa Securities Corporation
Incorporated under the laws of the State of New York

The undersigned hereby acknowledges receipt from Mrs. Mary E. Wilson of the sum of $3300.00 in full payment for subscription to thirty shares of the fully paid 6% cumulative preferred capital stock of the Iowa Securities Corporation.

After engraved stock certificates have been prepared, the holder of this receipt, upon surrender hereof, duly endorsed, at the office of the undersigned will be entitled to receive a certificate for the said preferred stock and a certificate for three shares of the fully paid common stock of the said corporation for every ten shares of preferred stock represented by this certificate.

Dated February 13, 1917,

Morgan, Truett & Company, Organization Managers, 40 Wall Street, New York City.

(Signed) Morgan, Truett & Company,

By E. P. Truett."

The false statement was a false statement in the representation of the ownership of the underlying securities, and the promise by the organization managers to deliver stock in the future, which was not owned, and which representation was false.

Said the Court (Circuit Court of Appeals Second Circuit, 1920):

"The argument of the appellee (objecting creditors) seems to be that the bankrupts obtained money upon the statement referred to; that they thereby obtained credit, and thereafter they obtained the money on credit upon the statement. But the language of the statute limits the refusal to discharge to obtaining money or property on credit upon a materially false statement in writing by him to any person or his representative for the purpose of obtaining credit from such person. It is plain that the intent of Congress was not to extend the statute to all cases of false written statements where credit happens to be given, and the thought being to confine the statute to cases where the decision to give credit was induced by the false statement. *Such statement must be a financial statement, as distinguished from a mere misrepresentation.*

"A debt fraudulently contracted by the bankrupt will not be released by his discharge. Therefore the debts in question, which the court below found were contracted fraudulently may fall within this provision of the Act. *Congress however, never intended to refuse a bankrupt his release from all his debts because he had contracted one or more fraudulently.*

"A discharge in bankruptcy is refused when

> the bankrupt has made false written statements as to his *financial* standing and thereby obtained money or property from any one relying on the statement * * * *
>
> * * * * We think Congress intended that the bankrupt should be discharged unless the statutory grounds of objection to the discharge are made out clearly."

The *Lundberg* case, *supra,* is from the Circuit Court of Appeals, Seventh Circuit, and holds that the false statement in writing must be a *financial statement.*

In that case the bankrupt made a false oath in his schedule, denying the ownership of certain property. The objecting creditor obtained a judgment and had a lien upon the property. The objection to discharge was because the bankrupt obtained from said judgment creditor the sum of $950.00 by giving a purported renewal judgment note for $800.00, upon which was written the words, 'being a lien on lots (to which false oath was taken he did not own)." The cause was reversed on appeal and the bankrupt discharged.

The *Robinson* case, *supra,* is from the First Circuit. Said the Court, in considering the history of the Act:

> "Legislative history of the amendment of 1910 to the Bankruptcy Act, by which Section

14 b (3) (Comp. St., Section 9598) was inserted in its present form, shows that Congress had in mind by a 'materially false statement in writing' the *statement of the debtor's financial condition* which he might make for the purpose of obtaining money or property upon credit. * * * *

A discharge should not be denied the bankrupt, unless for reasons specifically stated in the Act, and the statute should not be extended by construction.'

In that case the bankrupt drew a check upon a bank in which his account was overdrawn, obtaining money upon the check, and the discharge was by the District Court denied. The cause is reversed, the Court holding that the giving of the check upon a bank in which the account of the maker was overdrawn did not constitute a "materially false statement in writing," as contemplated by the Act, and the discharge should not be denied.

Said the Court:

'If the bankrupt had made an oral statement at the time the check was given that it was good or would be paid when presented, or that his account was overdrawn but that he had made arrangements with the bank on which it was drawn by which it would be paid, none of these oral statements would have been a bar to his discharge.

"We think it was the evident design of Congress to confine the objecting creditor to the limits of a specific statement in writing made by the bankrupt and that such statement cannot be extended beyond the fair and necessary meaning * * * * "

In the *Hudson* case, *supra,* the bankrupt obtained money on a note secured by a mortgage on a particularly described automobile. The bankrupt owned no such automobile. This was held *not* a ground to refuse a discharge under Section 4 b (3), that is, the discharge was granted, but the discharge of the bankrupt would not release the debt under Section 17, paragraph 2.

Said the Court:

"Congress would scarcely have provided that a debt or liability created by a given state of facts should be ground for objecting to a discharge and at the same time have excepted the debt so created from the discharge when granted. It is manifest that these two provisions, if so construed, would be inconsistent because, if an obligation so created was excepted from the discharge when granted, it could hardly be a ground for objecting to the granting of a discharge, which would not cancel or release such debt or liability."

The Court holds that while

An "analysis" of these facts presented by the situation in the instant case was 'that technically they do literally come within the provisions of sub-section 3' "; yet

" * * * * what Congres intended to do was to except from the effect of the discharge one class of debts or obligations created by obtaining property under false pretenses or false representations, as these words are used in the various statutes of the various states, making this state of facts a crime, and that the words used in Sub-section 3 of Section 14 were intended to be limited to such dealings between merchants or individuals *where a written statement of facts was made by the borrower as a basis of credit,* as ordinarily understood in mercantile dealings and that the language they have used when given its ordinary meaning, does just what Congress intended."

In the *Rea Bros.* case, *supra,* it was held that a check drawn on a bank in which the drawer had no funds but upon which he obtained the cash was not a "false representation in writing" under Section 14 b (3); this notwithstanding the fact that the Court expressly found that "the bankrupts purchased sheep, to be paid by check on delivery, which was done. They knew they had neither money nor credit on the bank of the check and it was dis-

honored when presented in due course."

> 'It is believed Congress by a 'false statement' altogether different in phrasology from, and importing false representations and more, intends the *financial statements* well known in the commercial *world,* setting out assets and liabilities, disclosing net worth and made to mercantile agencies and others, expressly as a basis for credit. In law statement generally means more than representations in that it deals with particulars or facts from which totals and conclusions may be computed rather than deals with mere totals or conclusions. The check is a false representation that the maker had sufficient money on deposit or had otherwise arranged so that the check would be paid on presentation but is not a 'false statement' within Section 14 as herein defined."

In the *Tanner* case, *supra,* Judge Rudkin held that the obtaining of a surety bond by a bankrupt by means of a materially false statement in writing covering his assets and liabilities was not the obtaining of property, and further quoting from *Firestone vs. Harvey,* 174 Fed. 574, says:

> "This ground for denying a discharge was evidently leveled particularly at the practice of making false statements of one's *financial condition* * * * *."

Collier, in his work on Bankruptcy, twelfth edition, at page 387, Volume I, discusses the matter with like result.

See also *Arnold vs. Smith,* 163 Northwestern 673, which shows that a discharge, if there was fraud, would not affect the debt here involved, as it could not be released under Section 17 Sub-division 2 or 4.

If a bankrupt obtains money upon a note secured by a mortgage and he does not own the property; if he obtains money upon a check drawn upon a bank in which he has no funds, or in which he knows his account is overdrawn; if he sells stock on a false prospectus and gives a receipt when he cannot deliver the stock sold, either in the future or at any other time, because of want of ownership; if none of these in the cases cited above constitutes "a materially false statement in writing," how can it be said that the receipts in this case fall under Section 14 b (3)? They are in no sense a financial statement of the condition of the bankrupt, nor do they show the status of his affairs. And these cases hold that any oral statements made at the time, even regarding his financial affairs, are immaterial touching the question of discharge, because the statute limits the objection to written, as distinguished from oral, statements.

Of course this argument is based upon the prop-

osition that the receipt is not ambiguous, and the widest latitude given to the testimony of the objecting creditors; that is, it assumes that credit was obtained upon these receipts, or money had thereunder, where the bankrupt had in his mind a knowing intent to deceive and where the lender was deceived. The negative of this proposition we will later discuss, but we contend here that in no sense do the receipts come under Section 14 b (3), but only, if at all, under Section 17-2-4, and no matter if the debts thus created will not be released, yet the Court cannot refuse a discharge to the bankrupt.

Let us look for a moment at that purpose of the Act:

> "A discharge is granted to an honest bankrupt in order that he may reinstate himself in the business world; it is refused to a dishonest bankrupt as a punishment for his fraud and to prevent its continuance in the future. Where a bankrupt has been brought into Court at the instance of his creditors, and all his property is being applied to the payment of his debts, he has paid the price of the discharge, and must be afforded the relief which he asks, unless he has been guilty of conduct, which, *under the Act,* deprives him of such relief."
>
> Collier, Twelfth Edition, Vol. 1, page 34;

In re Hammerstein, 189 Fed. 37;
Barton Bros. vs. Produce Co., 136 Fed. 355;
Herdie vs. Swafford etc., 165 Fed. 588;
Williams vs. U. S. Fidelity Co., 236 U. S. 549; 59 L. Ed. 713;
In re Oliner, 262 Fed. 734 (CCA);
In re Wood, 283 Fed. 565.

In the *Oliner* case, *supra,* the bankrupt obtained trust funds for transmission and deposited to his own account. The court held that "any tendency to make the Bankruptcy Act unduly harsh is to be avoided" and while the bankrupt might be punished under the State law, his discharge could not be refused.

In the *Wood* case, *supra,* it was held that the conversion by a bankrupt to his own use of goods consigned to him was no ground to refuse a discharge.

It cannot be contended that these receipts, in any sense, constitute a "financial statement." They were not made to a mercantile agency. No statement of assets and liabilities was required. Taking the strongest view against the bankrupt, as did the trial Court, these receipts were used and by their terms constituted the bankrupt the agent of the loanor.

> "The money was given for a specific purpose. It was for loan purposes * * * *. He

has not placed it into a general fund useful for a general purpose; and when he failed to do that, he violated a trust that was impliedly created, at least by these receipts." (Neterer, J. Trans. 15.)

Mr. Rummens: "Was it fraud or misappropriation?

The Court: "A misappropriation. He received money upon an implied understanding that a certain thing was to be done and it was not done." (T. 17.)

Clearly, that was not obtaining money or property on credit upon a materially false statement in writing, under Section 14, Sub-division 3, but if, as the District Court held, a relation other than debtor and creditor was raised, to-wit: principal and agent, and the money was "Misappropriated," then that situation falls squarely under Section 17, Sub-division 4:

"Or (4) were created by his fraud, embezzlement, misappropriation or defalcation while acting as an officer or agent in *any fiduciary capacity.*"

However, notwithstanding the statement of the Trial Judge, the testimony of the bankrupt and the books, uncontradicted, demonstrate that this money actually went into chattel loans. There was no misappropriation. The certain thing to be done was done.

On the assumption of "misappropriation" the debt itself may not be released but the discharge must be granted.

Says the District Court in the formal opinion:

> "I am satisfied from all of the testimony that the receipt or memorandum executed did not truthfully state the conditions upon which the money was paid to the bankrupt * * * *. The money was obtained by the bankrupt upon the receipt as the inducing cause which did not state the fact." (Trans. 19.)

Again, this is not the false statement warranting a refusal to discharge as shown by the above authorities but, if true, falls under Section 17, Subdivision 2:

> "Liabilities for obtaining property by false pretenses or false representations * * * *."

Strictly speaking, no money whatsoever was obtained upon these receipts but the receipts given in exchange for the money. The receipts were not made a financial statement as a basis of credit. They were simply the instrument employed to evidence the debt.

This argument has been based strictly upon the receipts themselves, excluding, for the moment, the testimony of the parties involved. Assuming that such testimony was admissable, which may be doubted under the above decisions, we will discuss that at a later point.

Now, assuming that we err in our argument and that the receipts do fall within Section 14 b (3), then the rule is:

> That the written statement made for the purpose of obtaining credit shall be knowingly and intentionally untrue in order to constitute a bar to the bankrupt's discharge; the bankrupt here must have intended to deceive at the outset.

3 R. C. L., page 311;

7 C. J. 377;

Franklin vs. Monning Dry Goods Co., 217 Fed. 929 (CCA);

Doyle vs. First National Bank of Baltimore, 231 Fed. 649 (CCA);

In re Kemp, 255 Fed. 125;

In re Goldberg, 256 Fed. 541;

In re Rosenfeld, 262 Fed. 876 (CCA);

In re Lundberg, 272 Fed. 107 (CCA);

W. S. Peck Co. vs. Lowenbein, 178 Fed. 178;

In re Stafford, 226 Fed. 127;

In re Collins, 157 Fed. 120;

In re Pfaffinger, 154 Fed. 528;

In re Cooper Grocery Co. vs. Gaddy, 141 Southwestern 825;

Hamilton vs. J. M. Radford Grocery Co., 182 Southwestern 716;

Allen-Wilms Jewelry Co. vs. Osborne, 231 Fed. 907;

In re Kenner, 250 Fed.993;

In re Troutman, 251 Fed. 930.

The rule is stated in the *Lundberg* case, *supra,* as follows:

> "But the law also is that, to bring the statement within that section it must have been intentionally and knowingly false and coupled with an intention to deceive."

In the *Rosenfeld* case, *supra,* it is stated:

> "The Bankruptcy Act is very liberal toward the bankrupt as to his discharge; and the Act in so far as it relates to his discharge is to be given a strict construction in favor of the bankrupt. The purpose of the Act is to release honest debtors from the burden of their debts.
>
> "The question then arises as to what is meant by a false statement. Does the word 'false' mean simply untrue, or does it mean wilfully and intentionally untrue? The answer is that the word as used in this connection means *designedly* untrue."

In the *Goldberg* case, *supra,* it is stated:

> "It is, of course, well settled that the statement must not only be false and material, but must be intentionally false, made with intent to deceive."

In the *Franklin* case, *supra,* where the discharge was denied and reversed on appeal, the court said:

"This section * * * * is intended for the beneficent purpose of discharging the honest bankrupt from the burden of his debts and thus allow him to begin his life anew * * * * This discharge is to be denied only when he is guilty of some one or more of the prohibited Acts * * * * It is not within the spirit of the objection that 'false' as used in the Act means simply 'untrue'."

This cause accepts the definition found in "Words and Phrases" as follows:

"'false' means that which is not true, coupled with a lying intent."

It also accepts the definition of Collier:

"Intent to deceive is always material as an element of proof and by the weight of authority it is essential to prove such intent."

So the Court concludes:

"We therefore have reached the conclusion that the word 'false' as used in clause 3 of Section 14 b of the Bankruptcy Act, means more than untrue, erroneous, or mistaken, but means 'false' in the sense that it is *'intentionally untrue'.*"

This rule was followed in the *Doyle* case, *supra,* where it is said:

"The decisions are in substantial harmony in holding that the bar to a discharge by reason

of a false statement in writing is confined to such person or persons as actually make such statement with the *intent to deceive.*"

The above rule of law should be borne in mind in considering the question of burden of proof.

The burden of proof was upon the objecting creditors to establish their objections by clear and convincing evidence.

In re Troutman and Jesse, 251 Fed. 930;
2 Loveland on Bankruptcy (Fourth Edition, Sec. 736);
Collier on Bankruptcy, Twelfth Edition, Vol. 1, page 362;
In re Kolster, 146 Fed. 138;
In re Walder, 152 Fed. 489;
In re Wix, 236 Fed. 262; 240 Fed. 692;
In re Lally, 25 Fed. 358;
In re Garrison, 149 Fed. 178;
Hardie vs. Swafford etc., 165 Fed. 588;
In re Cohen, 206 Fed. 457;
In re Miller, 212 Fed. 920;
Poff vs. Adams, 226 Fed. 187;
In re Main, 205 Fed. 421;
In re Johnson, 215 Fed. 748;
In re Shrimer, 228 Fed. 794;
In re Haimowich, 232 Fed. 378;
Shemberg vs. Hoffman, 236 Fed. 343;
In re Braun, 239 Fed. 113;
In re Garrity, 247 Fed. 310;

Horner vs. Hammer, 249 Fed. 134;

In re Spiropolis, 292 Fed. 745.

In the *Troutman* case, *supra,* the syllabi is as follows:

"A creditor objecting to discharge on the ground that the bankrupt obtained credit on a false financial statement, has the burden of establishing that fact by clear and convincing evidence and unless the burden is met, discharge should not be denied."

Loveland states the rule:

"The burden of proof is on the objecting creditor to establish by clear and convincing evidence his objection."

Collier says:

"Proof must be strict and convincing, but not necessarily to the limit required in proving a crime * * * * The burden of proof is upon the opposing creditor * * * *.

"It is not necessary that the alleged ground for refusing a discharge be proved beyond a reasonable doubt, as in the case of the trial of a criminal offense, although the conscience of the Court should be satisfied by clear and convincing testimony that the bankrupt is not entitled to a discharge."

In the *Kolster* case, *supra,* it is said:

"The most that can be said is that the cir-

cumstances 'look suspicious.' This is not enough. Mere conjecture or surmise is not sufficient."

The case holds that the proof must be inconsistent with honesty and fair dealing.

In the *Walder* case, *supra,* the Court said:

> 'The burden of proof to sustain the alleged specifications is upon the creditors that filed the same, and that burden never shifts."

In the *Wix* case, *supra,* the Court says:

> "The discharge is a very great privilege and right * * * *. The burden rests upon the creditors objecting * * * *.'

In the *Lally* case, *supra,* we find this language:

> "* * * * The evidence must be clear, convincing and satisfactory. It is not enough that strong suspicion is created by the testimony. The inference must be such as to carry conviction."

Applying the above rules to the facts in this case, how can it be said that the bankrupt at the time the loan was obtained had the wilful intent to

then deceive and did not intend to make the loans or pay back the money borrowed? This is particularly true when there is borne in mind the fact that the bankrupt turned over to his assignees property he believed of a then value of $140,000.

Under the testimony of the bankrupt, this was a direct loan and nothing else. There is no dispute

but that he was in the loan business and he testifies that as a matter of fact this money went into chattel loans wherein he lost twenty-nine thousand dollars. But for that loss, the money would have been repaid; but for that loss, connected with his other losses, he would not have been bankrupt. As a matter of fact if the assignees had been permitted opportunity to work out the assets turned over to them there would have been no bankruptcy forced upon appellant.

The objecting creditors frankly admit, on direct examination, that the money was a "loan" to the bankrupt. However, they assert that they would not have loaned him the money if they had known he was going to use it in his personal business.

There is no evidence that he did use it in his personal business. These creditors had access to the books of the bankrupt and had such access for a period of three years. The books were in court. They showed that this money went into chattel loans.

It is true the bankrupt considered that the loan was made to him and that he could use it as he saw fit, but he was in the chattel loan business and was borrowing money to use in the chattel loan business. That is where this money was used and there is no evidence to the contrary, except the statement of Mrs. Helm, contradicted by the bankrupt and by

the books, that he stated to her he had used it personally. From his standpoint and understanding he could have used it personally but did not. The giving of these receipts in this form was the idea of the bankrupt. It is not denied but that Mrs. Helms requested a promissory note rather than a receipt, but at the suggestion of the bankrupt, took a receipt. Unquestionably, if there had been delivered to her the piece of paper which she requested, to-wit: a promissory note, and the very fact of that request demonstrates that she considered it a straight loan, there could have been no question of the right of the bankrupt to discharge because the controversy would not have arisen; but he gave receipts, and the creditor now takes the position that he was to loan the money for her—in other words, that a trust was established and that the bankrupt violated the same.

If this be so, what was the consideration moving to the bankrupt from the principal? The bankrupt was paying interest upon this money at the rate of 10%. The maximum rate of interest in this District is 12%. While the money was loaned for a six months' period, the bankrupt agreed to repay the same at any time upon two weeks' notice in advance. The thousand dollar loans were changed into five hundred dollar receipts coming due at different times so he might the more readily repay. She knew he could not loan her money on any such

basis. How can it be contended that the bankrupt could use this money upon chattel loans, wherein he would subject it to such termination, unless it was considered a straight loan to himself?

Again, the creditor does not claim that the money was to be loaned in her name; that she ever inquired as to what security was taken, its form, substance or nature; that she ever asked to see a single paper or document; that she ever made any inquiry whatsoever as to any loan, except that after loaning Six Thousand Dollars she claims she was very careful to see that a Three Hundred Dollar loan was made upon a house boat. The very substance of her testimony upon the latter proposition weakens her testimony upon the former.

Then, where in this record have the objecting creditors sustained the burden of proof that was upon them? The testimony of the bankrupt is consistent with honesty and fair dealing. We contend that the circumstances did not "look suspicious"; even so, under the above authority, "mere conjecture or surmise is not sufficient."

It must also be borne in mind it is undisputed that these receipts were the customary form that the bankrupt used in his business dealings over a long term of years and that he considered them a straightforward transaction and a satisfactory method of handling the business. This of itself is of

some importance.

In the case of *"In re Goldberg,"* 256 Fed. 541, the Court says in a case where a statement upon which credit was obtained was false: "It is settled that intentional dishonesty is a necessary element * * * *." The case holds that the presumption from the false writings themselves is not conclusive and is rebuttable by the fact that such means employed was the ordinary custom of the bankrupt in his business and material in showing lack of intent to deceive.

The fact that certain of the creditors who originally opposed the discharge have abandoned their position is likewise entitled to consideration by the Court if there is doubt as to the bankrupt's guilt. (7 Corpus Juris 792.)

The record in this case shows that the principal objecting creditor, Mrs. Helms, prosecuted the bankrupt in the State Courts upon a criminal complaint in this same matter and the jury found him not guilty.

Under the facts and circumstances, is there not every reason to doubt the guilt of the bankrupt? Can it be said that there is evidence clear and convincing that shows that necessary intent to deceive; that shows the receipt to have been intentionally untrue; that shows the act of the bankrupt to have been designedly false; that shows the wicked heart

necessary to convict in such a case?

The Trial Judge should have granted the motion of the bankrupt for a non-suit and thereupon entered an order of discharge at the close of the case of the objecting creditors, because there was no testimony at that time in the record going beyond the face of the receipts or any showing whatsoever that a financial statement had been made, or that the receipt was a materially false statement in writing and money or property obtained upon it.

If there could have been any doubt in the mind of the Trial Judge at that stage of the case, it must have been removed by the uncontradicted testimony of the bankrupt, supported by his books showing that the money was actually lost in chattel loans; but over and beyond that, as between the parties themselves, it was considered a loan—no more and no less—and the objecting creditors so considered it, because they desired promissory notes in the place of the form receipts.

As a matter of law the Court should have held that the receipts did not fall under Section 14, and it was not required to pass upon whether or not the debts thereby created would or would not be discharged under Section 17.

In the absence of fraudulent intent, all the money having been used in the loan business, even though it may have been accepted as a trust as

assumed by the Trial Judge inasmuch as the terms of the trust were carried out, how can there be liability, either civil or criminal, on the part of the agent?

We submit that when there is borne in mind the beneficent purposes of the Bankruptcy Act; when a great majority of the creditors, both in numbers and in amount, are seeking the discharge of the bankrupt; when there is kept in mind the great distinction existing between the right to a discharge under Section 14 b, as distinguished from those debts not released in bankruptcy under Section 17-2-4, the discharge must be granted in this case, and the question of the release of the particular debts here involved left for future consideration, as by the Acts provided.

If, on the other hand, it be determined that the statement involved is not of necessity a financial statement, and that by a wide latitude of construction under Section 17-b and contrary to all of the decided cases these receipts are such as are contemplated by the section, and the discharge may be refused, then we submit that the objecting creditors have not sustained the burden of proof by clear and convincing evidence that there was the designedly false and fraudulent intent necessary to defeat the right of the bankrupt to his discharge.

SPECIFICATION 7.

If we err in our conclusion that the bankrupt is entitled to his discharge, and this court hold with the District Court that the objections were well taken, we are then met with this situation:

Creditors with claims aggregating $72,950.35 desire that the bankrupt be discharged. The greater portion thereof have specifically petitioned and joined in the application for discharge. Because of the existence of the claims of two creditors, in an amount of $4,190.00, a discharge is denied.

Let it be assumed for the sake of argument that our position is wrong in the original Specifications of Error, and a discharge should be refused the bankrupt as to the debts of these two objecting creditors; but should the other creditors, with claims aggregating thousands of dollars be likewise penalized, simply because these two have asserted a claimed technical right? For, not only is the bankrupt penalized, but there is likewise penalized all the creditors who seek his discharge, because, in refusing same to the bankrupt, any hope they may have in the future, of obtaining from the debtor that which is due as a moral obligation, is destroyed forever.

It could not have been the intention of Congress to thus indirectly destroy both the legal and moral right of the creditors otherwise affected.

Surely no reason can be found in the Act as to why the discharge should not be limited as well as general. The opinion (Trans. 19) cites but one case to the contrary *in re Miller*, 192 Fed. 730, and while that case and those upon which it relies has taken a contrary position, we submit it has overlooked the harm resultant to the parties whom the Act intends to protect, as well as the bankrupt. A limited discharge might be denied a voluntary bankrupt but should the same rule apply to one whose act is involuntary?

If our conclusions be wrong, then if this bankrupt had failed with liabilities of $10,000,000, without sufficient assets to meet them, and every transaction had been without the statute, except he had obtained $10.00, or 10c, on a receipt such as is here involved, the discharge would be denied, which, to us, goes back to the provision that the District Court misconceived the distinction between Sections 14-b and 17 and that the case at bar falls, if anywhere, under Section 17-2 or 4.

As the cases we have cited point out, it was not the intention of Congress and is not the intention of the law to deny a discharge to a bankrupt simply because certain of his debts have been fraudulently contracted. It was the intent to prevent the discharge of such debts. As the matter works out in human experience, and in business dealings, it is

better for the very creditors who may have been defrauded that the bankrupt, having lost all his gains, if any, and perchance his reputation as well, should go forth with the opportunity of making an honest living and paying such debts. If they are not released, they are still collectible from the bankrupt when he again enters a gainful occupation. If he be denied his discharge, then not only those creditors, but those others to whom the moral obligation still remains to pay an honest debt, will never be paid, because the refusal of a discharge is a life sentence removing a man from all possibility of ever again rehabilitating himself, and bars him from the opportunity of earning a livelihood.

We submit that under the Act, as construed by the above decisions, under the facts in this case, and in equity and good conscience, the bankrupt should be granted a discharge, as prayed.

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